

Office of Chief Counsel
Internal Revenue Service
memorandum

CC: [REDACTED]: POSTF-159763-01
[REDACTED]

date:

to: LMSB Financial Products & Transactions Team
Manager [REDACTED]
Attn: Financial Products Specialist [REDACTED]

from: Associate Area Counsel (LMSB/2), [REDACTED]

subject: [REDACTED]

This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse effect on privileges, such as the attorney-client privilege. If disclosure becomes necessary, please contact this office for our views.

This memorandum is submitted in response to Financial Products Specialist Denise Thomason's request for our views concerning a potential argument that she seeks to raise in the above-referenced case to disallow some \$ [REDACTED] in losses that the taxpayer claimed between the years [REDACTED] and [REDACTED] on the ground that the losses must be deferred because they arose from the sale of receivables to a related entity in accordance with I.R.C. § 267.

ISSUE

Whether the taxpayer is entitled to claim some \$ [REDACTED] in losses from the sale of its receivables to a subsidiary.

CONCLUSION

The losses are barred by section 267 until such time as the receivables are transferred outside the controlled group and the loss would be recognized under consolidated return principles.

FACTS

[REDACTED] (the taxpayer) is a diversified manufacturer of engineered products and components with annual revenue of \$ [REDACTED]. The taxpayer's sales and production are focused in the [REDACTED]
[REDACTED]

On [REDACTED], the taxpayer, after a number of transactions, transferred receivables and all of the stock of [REDACTED] to another of the taxpayer's subsidiaries, [REDACTED]. On that same date, [REDACTED] transferred receivables to [REDACTED], a controlled foreign corporation. [REDACTED] and [REDACTED] then transferred assets with a fair market value of \$ [REDACTED] to [REDACTED] in exchange for all ([REDACTED]) of the shares of [REDACTED]'s common stock. At the end of the day, [REDACTED] owned [REDACTED] percent ([REDACTED] shares) of [REDACTED]'s common stock and [REDACTED] owned [REDACTED] percent ([REDACTED] shares) of [REDACTED]'s common stock. It is our understanding that the taxpayer owned [REDACTED] percent of both [REDACTED] and [REDACTED].

On [REDACTED], [REDACTED] and the taxpayer entered into a Receivables Purchase and Sale Agreement, under which [REDACTED] agreed to purchase the eligible receivables of the taxpayer and its subsidiaries. On its consolidated income tax returns for the years [REDACTED], [REDACTED], and [REDACTED], the taxpayer claimed losses in the respective amounts of \$ [REDACTED], \$ [REDACTED], and \$ [REDACTED] from the sale of the receivables to [REDACTED].

The Financial Products Specialist proposes to disallow the losses that the taxpayer claimed from the sale of the receivables to [REDACTED] under I.R.C. § 267.

DISCUSSION

In general there is nothing to prevent a taxpayer from selling or exchanging property for the sole purpose of establishing a tax loss, provided the sale is bona fide and the loss results from a closed transaction. I.R.C. § 267, however, adds a special exception to this general rule where a sale or exchange at a loss takes place between certain related parties. Specifically, section 267(a) provides that, except in the case of

a distribution in complete liquidation, "[n]o deduction shall be allowed in respect of any loss from the sale or exchange of property, directly or indirectly, between persons," specified in section 267(b). Such persons include, inter alia: "two corporations which are members of the same controlled group (as defined in subsection (f))." I.R.C. § 267(b)(3).

As relevant here, for purposes of section 267 a "controlled group" is defined as one or more chains of corporations connected through stock ownership with a common parent if: (A) stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote or more than 50 percent of the total value of shares of all classes of stock of each of the corporations, except the common parent is owned (within the meaning of subsection 1563(d)(1)) by one or more of the other corporations; and (B) the common parent corporation owns (within the meaning of subsection 1563(d)(1)) stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote or more than 50 percent of the total value of shares of all classes of stock of at least one of the other corporations, excluding, in computing such voting power or value, stock owned directly by such other corporations. See I.R.C. § 267(f)(1).¹

During the years [REDACTED], [REDACTED], and [REDACTED], [REDACTED] owned [REDACTED] percent of [REDACTED]'s common stock, [REDACTED] owned [REDACTED] percent shares) of [REDACTED]'s common stock, and the taxpayer owned [REDACTED] percent of both [REDACTED] and [REDACTED]. Thus, the losses claimed from the sale of the taxpayer's receivables to [REDACTED] in [REDACTED], [REDACTED] and [REDACTED] are barred under section 267. Accordingly, the taxpayer is required to defer the losses until such time as the receivables are transferred outside the controlled group and the loss would be recognized under consolidated return principles. See I.R.C. § 267(f)(2).

¹ For purposes of section 267, the term "controlled group" has the same meaning given to that term in I.R.C. § 1563(a), with two modifications: (A) more than 50 percent is substituted for at least 80 percent each place it appears in section 1563(a), and (B) the determination is to be made without regard to subsections (a)(4) and (e)(3)(C) of section 1563. See I.R.C. § 267(f)(1).

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Please contact the undersigned at [REDACTED] if you have any questions or concerns regarding this memorandum.

[REDACTED]
Associate Area Counsel
(Large and Mid-Size Business)

By: _____
[REDACTED]
Senior Attorney (LMSB)

cc: Financial Products Specialist [REDACTED]

cc: LMSB Counsel, [REDACTED]